No. 12961

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

HERSCHEL BULLEN, MARY H. BULLEN, J. C. HAYWARD and MARY S. HAYWARD,

Appellants,

vs.

ADAMANT COMPANY, WALTER B. SCOVILLE, JOE SEEPLE and HARRY WYNN; UNITED STATES OF AMERICA and RECONSTRUCTION FINANCE CORPORATION,

Appellees.

Reply Brief of Adamant Company, Walter B. Scoville, Joe Seeple and Harry Wynn, Appellees.

LELAND J. ALLEN,
1200 Title Guarantee Building,
411 West Fifth Street,
Los Angeles 13, California,
Attorney for Adamant Company, Walter B. Scoville, Joe Seeple and Harry Wynn, Appellees.

Parker & Company, Law Printers, Los Angeles. Phone MA 6-9171

TOPICAL INDEX.

PAGE

Statement of facts 1

Argument 4

Conclusion 15

TABLE OF AUTHORITIES CITED.

Cases	PAGE
Austin v. Hallmark Oil Co., 21 Cal. 2d 718	8, 9
First National Finance Corporation v. Five-O-Drilling Co., 209 Cal. 569	12
Gapes v. Salmon, 35 Cal. 576	13
Helvering v. O'Donnell, 303 U. S. 370	10, 15
Morrison v. Havens, 24 Cal. App. 2d 504	11
Recovery Oil Co. v. Van Acker, 79 Cal. App. 2d 639, 96 Cal. App. 2d 909	4, 5, 6

No. 12961

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

HERSCHEL BULLEN, MARY H. BULLEN, J. C. HAYWARD and MARY S. HAYWARD,

Appellants,

vs.

ADAMANT COMPANY, WALTER B. SCOVILLE, JOE SEEPLE and HARRY WYNN; UNITED STATES OF AMERICA and RECONSTRUCTION FINANCE CORPORATION,

Appellees.

Reply Brief of Adamant Company, Walter B. Scoville, Joe Seeple and Harry Wynn, Appellees.

Statement of Facts.

Findings XXIV and XXV [R. 145, 146] correctly state the facts: That to obtain funds to complete the well, Walter B. Scoville entered into an agreement with Herschel Bullen and wife and J. C. Hayward and wife, whereby the Bullens and the Haywards agreed to contribute, and did contribute, $2,500.00 per couple to be used in completing the well, and said money was so used, and in consideration of such advancement of funds, Walter B. Scoville agreed to assign to each couple a one per cent interest. Said Scoville agreed with said parties that

the sums so advanced were to be repaid to them "two for one." The assignments from Walter B. Scoville to the Bullens and Haywards were assignments of the leasehold and not of only oil produced, saved and sold.

Walter B. Scoville agreed to return the money advanced by the Bullens and the Haywards "two for one" out of the first 15 per cent of gross production of the well. This agreement was made for the sole purpose of obtaining sufficient money to complete the well.

The plan as evolved by Walter B. Scoville was approved by the Adamant Company and the Treasure Company. The Treasure Company and the Adamant Company consented to the transferring of a part of said Scoville's interest, and agreed that said Scoville could raise the necessary finances as proposed.

Neither the Treasure Company nor the Adamant Company executed said agreement between Walter B. Scoville and the Bullens and the Haywards as parties, nor were said Treasure Company nor the Adamant Company parties thereto, nor were said Treasure Company nor the Adamant Company bound thereby.

The appeal by Bullen and Hayward involves the following points:

1. Whether or not an agreement to pay a bonus of "two for one" out of oil constitutes a royalty.

2. Whether or not said bonus agreement created an equitable lien, or simply a personal contract between Bul-

len and Hayward and Walter B. Scoville with no liability on the part of Treasure Company or Adamant Company.

3. Whether or not said bonus contract created any lien against the interests of Walter B. Scoville, or any other claimants, of moneys due under the award.

4. Whether or not the working interests were alone covered by the jury verdict, and hence said jury award should be divided equally among the working interests of 80.6 units and not into 100 units, which latter division gave Treasure Company more than it really owned.

5. Whether or not the portion of the jury award belonging to the lessee and operator (or his belated assignee) is subject to an equitable lien for funds due the owners of working interests who received none of the net profits of the well by reason of said lessee and operator refusing to pay over said profits.

6. Whether or not the court erred in reducing the award by the amount of the Master's fee in the Accounting case, insofar as that deduction applies to Bullen and Hayward.

ARGUMENT.

At page 15 of the Bullen and Hayward brief there is this statement:

"The Two for One Agreement is a royalty."

The Two for One Agreement could *not possibly be* a royalty because there are only one hundred oil royalties in a lease.

In the case at bar the landowners' royalty amounted to 19.4 units. [R. 746.]

The working interests amounted to 80.4 units.

This comprised all of the *possible royalties* that could be outstanding upon this leasehold.

The Two for One Agreement is *simply a contract* but not a royalty.

There is a vital distinction between the assignments construed in the case of *Recovery Oil Co. v. Van Acker,* 79 Cal. App. 2d 639, and the same case found later in 96 Cal. App. 2d 909. (Cited pp. 15-20 of Bullen and Hayward brief.)

The *assignments* construed in those two cases read as follows:

> "On November 20, 1928, A. Bruce Frame and his wife executed the following written assignment:
>
> "That, referring to that certain Oil and Gas Prospecting Permit, Visalia Serial 010101, M. A. Knapp, Assignee, and referring to the Operating Agreement dated May 2, 1928, executed by said M. A. Knapp to the undersigned, covering the following described premises: (Description.)
>
> "The undersigned hereby assigns, transfers and sets over to N. E. Grable the proceeds from Fifteen

percent (15%) of the oil, gas and other hydrocarbon substances produced, saved and sold from the said premises so covered by said Operating Agreement (less amount used in operations on the premises), until such time as said assignee shall have received the sum of Twenty Thousand Dollars ($20,000.00) and no more; and upon full payment of said sum this assignment shall terminate and be at an end."

On April 10, 1929, N. E. Grable executed the following instrument:

"In Consideration of the receipt, by the undersigned, of Ten and no/100 ($10.00) Dollars, N. E. Grable, unmarried, of Los Angeles County, State of California, does hereby remise, release, assign and Quitclaim to Ada M. Crawford of Los Angeles County, State of California, the following: *This instrument is intended to transfer all right, title and interest now held by the Grantor* in and to one half (½) *of the interest acquired* by the Grantor under that certain instrument dated November 20, 1928, and recorded November 27, 1928, in Book 272, Page 431 of Official Records of Kern County, California, without any warranty or assurance of title whatsoever." (Emphasis added.) (P. 640 of 79 Cal. App. 2d.)

In the *Van Acker* case, *supra,* the interest created by the assignments constituted a direct proportion of the oil, gas and other hydrocarbon substances.

The second assignment above, being the one from Grable to Crawford, states:

"This instrument is intended to transfer all right, title and interest *now held* by the grantor * * *."

Bullen and Hayward received two units of royalty out of the total of 100 units possible in an oil lease *at the time* they paid their money. Such being the case the contract to pay for "Two for One out of oil" was in the nature of a bonus and, of course, their 2 per cent royalty was benefited by their investment just as much in proportion as the other 98 unit holders in the leasehold.

Furthermore, in the *Van Acker* case the 15 per cent royalty *was included* within the 100 per cent or 100 units of royalty in the leasehold.

We quote from page 910 of the Final Decision of *Recovery Oil Co. v. Van Acker,* 96 Cal. App. 2d 909, as follows:

> "Various partial assignments of said lease were made to others and in 1938, the plaintiff became the owner of Knapp's *remaining interest* in this lease insofar as it pertained to the land here involved."

The above quotation indicates in using the words "remaining interest in this lease" that such remaining interest referred to the difference between the outstanding per cents and 100 per cent.

We again quote from the final decision in the *Van Acker* case as follows (96 Cal. App. 2d 909-911):

> "A judgment in favor of the plaintiff was reversed on appeal (Recovery Oil Co. v. Van Acker, 79 Cal. App. 2d 639 (180 P. 2d 436)) for reasons not involved here. After a retrial the court found, so far as material here, that the oil and gas lease given to Knapp in 1930 was subject to the *operating agreement* between Knapp and Frame, and to the *assignments above referred* to from Frame to Grable and *from Grable to Ada M. Crawford;* that the plaintiff

became the owner of so much of Knapp's *interest* in the *property* as remained *after* these transfers and assignments; that each of these transfers and assignments were duly recorded and plaintiff had constructive notice thereof; and as a conclusion of law, that the plaintiff's lease, insofar as this property is concerned is subject to a valid assignment now held and owned by Ada M. Crawford whereby she is the owner of 15 per cent of the proceeds of the oil etc., saved and sold from the premises until such time as she shall have received $10,000.00, whereupon her interest shall terminate and be at an end. Judgment was entered accordingly. The plaintiff appealed from the entire judgment, but prosecutes this appeal only from that portion thereof which sustains the claim of Ada M. Crawford." (Emphasis added.)

The above clearly indicates that there can be no royalty interests in excess of 100 per cent or of 100 units.

When Bullen and Hayward received the written assignment of one per cent each said assignment read, in part, as follows:

"* * * sell, assign, set over, transfer and convey to Herschel Bullen and Mary H. Bullen as joint tenants * * * one per cent participating royalty interest in all oil, gas and other hydrocarbon substances produced, saved and sold from the following described premises, * * *." [See Finding XVII; R. 141.]

Bullen and Hayward knew by *comparing* their respective assignments of a one per cent participating royalty with the *bonus* contract that the two were *entirely different* and that while the one per cent assignment of a royalty gave them an equitable lien, as it transferred to them a

capital *investment* in the production of oil and gas the bonus contract gave them no such rights.

Each contract is governed by the intent of the parties to said contract.

This bonus contract was never intended to be a participating royalty interest, otherwise it would have been so worded.

Bullen and Hayward quote from the case of *Austin v. Hallmark Oil Co.,* 21 Cal. 2d 718, at page 18 of their brief.

The basis of the decision in said case was an oral grubstake agreement, such agreements having always given the party who grubstaked the other party a definite interest in the *"res"* or property obtained.

We quote from the *Austin v. Hallmark Oil Co.* case:

> "On November 2, 1934, in accord with the *obligation imposed* by the grubstake agreement of July 1st, Porter assigned to Austin one-half of all income, profits, moneys and credits to become due or payable to him under the terms of his contract with the Hallmark Oil Company, Inc." (P. 723.)
>
> * * * * * *
>
> "The interest created by an assignment depends upon the *intention of the parties* (La Laguna Ranch Co. v. Dodge, 18 Cal. 2d 132 (114 P. 2d 351, 135 A. L. R. 546); National R. Co. v. Metropolitan T. Co, 17 Cal. 2d 827 (112 P. 2d 598); Callahan v. Martin, 3 Cal. 2d 110 (43 P. 2d 788, 101 A. L. R. 871)), and while that intention is determined primarily from the terms of the instrument, the language of the assignment must be construed in the light of

the facts and circumstances of the particular case. (Schiffman v. Richfield Oil Co., 8 Cal. 2d 211 (64 P. 2d 1081); Adamson v. Paonessa, 180 Cal. 157 (179 P. 880).) (13) In view of this rule it is clear that the instrument in the present case was intended to transfer fifty per cent of the interest retained by Porter under the agreement of October 30th, regardless of the nature of that interest. *By virtue* of the *grubstake agreement,* Austin was equitably entitled to such a share, and since the intention to confer rights different from those previously held is not manifested by the terms of the assignment, it must be assumed that Porter intended it to fulfill the obligations *of his trust."* (P. 730.) (Emphasis added.)

Austin v. Hallmark Oil Co., 21 Cal. 2d 718, 723, 730.

The *Hallmark* case clearly holds that the assignment of a right created by a grubstake agreement carries the interests obtained by the grubstake agreement.

A bonus contract is not in the same category as a grubstake agreement.

It was stipulated that the proceeds from the production of the oil well, amounting to $205,411.68, was handled by the Treasure Company. [R. 1236.]

Neither Mr. Scoville nor the Adamant Company received a penny of said production moneys.

The United States Supreme Court has definitely ruled that a contract such as this one (whether we call it a bonus or not), does not create an equitable lien.

In the case of *Helvering v. O'Donnell,* 303 U. S. 370 (1937), the Supreme Court said:

> "The question is whether Respondent had an interest, that is, a capital investment in the oil and gas in place."

The case turned upon the point that:

> "The agreement to pay Respondent one-third of the net profits derived from the development and operation of the properties was a *personal* covenant and did not purport to grant Respondent an interest in the properties themselves. If there were no net profits, nothing would be payable to him. No trust was declared by which Respondent could claim an equitable interest in the *res.*" (303 U. S. 372.)

The Appeals Court of California denied an equitable lien in a similar contract situation.

We quote:

> "The complaint was based upon a written instrument alleged to have been executed by John Weston Havens in 1903 in words and figures as follows:
>
> " 'Berkeley, Cal. Jan. 6th, 1903.
>
> " 'To whom it may concern, and especially my executor—
>
> " 'It is agreed that I shall pay out of the sale of Block 22 Shattuck Tract number 5, the macadamizing bill of $617.41 and grading bill of $349.72.
>
> " 'J. W. Havens.'
>
> "From the prayer of the complaint and the briefs, it appears that plaintiff was seeking to have it declared that said instrument created an *equitable lien* upon said real property and upon the proceeds of any

sale of said property which might be made at any time.

"(1) Appellant contends that his complaint stated a cause of action for such declaratory relief and that the trial court erred in sustaining the general demurrer thereto. *We find no merit in this contention.* The instrument in question manifests no intention to create a lien upon the real property. It appears to be an informal memorandum executed for the purpose of evidencing the personal obligation of the maker. Said obligation was to be paid by the maker or his executor, to whom a claim might be presented, but payment was deferred until the time of sale of the property. At most it was a mere agreement to pay a debt out of a particular fund, when received, but *such an agreement does not create a lien even upon such fund.* (Maier v. Freeman, 112 Cal. 8 (44 Pac. 357, 53 Am. St. Rep. 151); 37 Cor. Jur., p. 314, sec. 15; also, p. 318, sec. 21.)" (Emphasis added.)

Morrison v. Havens, 24 Cal. App. 2d 504 (1938).

(Supreme Court denied petition for hearing March 25, 1938.)

The mere fact that Bullen and Hayward received an assignment of 2 royalty units put them on notice that their contract calling for two for one out of production was not a royalty interest but a plain contract for a bonus.

We cannot agree with Bullen and Hayward that:

"The Van Acker case is, therefore, on all fours with the case at bar, * * *." (Br. p. 19.)

We submit:

The Two for One Agreement is not a royalty agreement.

* * *

At page 22 the Bullen and Hayward brief states:

> "The two for one agreement is binding on all owners of the working interests."

It has been stipulated in the case at bar that Treasure Company handled all of the proceeds from the production of the well prior to the time of its seizure by the Government in the condemnation proceedings. [R. pp. 1235-1236.] In view of that fact, if any one is liable for the payment of the two for one, it would be the Treasure Company alone.

Other owners of working interests did not become liable under the contract. They acquired their interests and paid for same without any obligation to pay any bonus.

In *First National Finance Corporation v. Five-O-Drilling Co.,* 209 Cal. 569, the Court states:

> "The transaction leading to the institution of this suit having been carried on by Kelley in the *ordinary course* of the business of the appellant, it may not now *deny his authority* in the premises."

Naturally the Supreme Court ruled as quoted at page 24 of the Bullen and Hayward brief.

We submit that appellants have failed to show any contract pledging any working interests as collateral for the fulfillment of the two for one agreement. *Hence no working interest is liable under the bonus contract.*

* * *

Bullen and Hayward state at page 27 of their brief as follows:

> "The two for one agreement is at least a charge on the interest of Walter B. Scoville."

We fail to find in the record any pledge of the interests of Walter B. Scoville as guaranteeing fulfillment of the Two for One Agreement.

In view of the fact that Walter B. Scoville handled *none* of the proceeds from the production of oil there can be no lien upon any of his interests, since *he* did not misapply any of the proceeds.

Gapes v. Salmon, 35 Cal. 576, 587, 588 (cited p. 28 of the Bullen and Hayward brief), held as follows:

> "The rule upon this point is, that one tenant in common cannot convey any specific part of the land so as to prejudice his co-tenant." (Cases cited.) (P. 587.)

In the case at bar Scoville did not convey anything in the bonus agreement hence the citation of the above case is not in point *even by analogy.*

We submit that any interests held by Walter B. Scoville were free from any pledge as collateral and hence not chargeable with the two for one bonus agreement.

* * *

At page 28 Bullen and Hayward state in their brief as follows:

> "The Appellants Bullen and Hayward and other holders of *participating royalties* have an equitable lien upon the interest in the well of the lessee, Treasure Company, to secure the payment to them of their share in the net proceeds of operation."

The Adamant Company, Walter B. Scoville, Joe Seeple and Harry Wynn agree fully with the above contention as to the 2 per cent participating royalty belonging to Bullen and Hayward and respectfully refer this Court to their Opening Brief *as appellants* where the equitable lien is fully discussed at pages 28 to 44 inclusive of said brief.

* * *

At page 36 of the brief Bullen and Hayward state:

> "The Reconstruction Finance Corporation, as the successor of Treasure Company, is bound by the lien."

We agree fully with his and refer the Court to the above reference of our Opening Brief as Appellants.

* * *

We also agree with the statement of Bullen and Hayward at page 36 of their brief, reading as follows:

> "Appellants Bullen and Hayward are entitled, by virtue of their ownership in the aggregate of a 2 per cent participating royalty to receive 2/80.6 of the award."

These appell*ees* refer this Court to their Opening Brief as Appellants, and specifically to pages 16 to 27 thereof discussing this same situation.

Conclusion.

As to the appellants Bullen and Hayward:

1. They are entitled to an equitable lien against any funds to be allocated to Treasure Company or its belated assignee Reconstruction Finance Corporation, to the extent of 2 per cent of $205,411.68 less cost of operation and *less any moneys heretofore received* by them from Treasure Company, as shown by the evidence before Judge Westover.

2. Bullen and Hayward are entitled to no equitable lien against any funds by reason of their bonus contract, as said alleged contract gave them no interest in the *"res"* as stated by the United States Supreme Court in *Helvering v. O'Donnell,* 303 U. S. 370.

3. It is the *"res"* that was distributed by the trial court and Bullen and Hayward have no claim or lien upon any of the *"res"* except 2 per cent thereof.

Respectfully submitted,

Leland J. Allen,
Attorney for Adamant Company, Walter B. Scoville, Joe Seeple and Harry Wynn, Appellees.